UNITED STATES DISTRICT COURT

DISTRICT OF PUERTO RICO

Ambac Assurance Corporation,	)	Docket No. 3:20-AP-00068(LTS)
	)	
	)	*in 3:17-BK-3283(LTS)*
Plaintiff,	)	
	)	
v.	)	January 12, 2021
	)	
The Financial Oversight and Management Board for Puerto Rico,	)	
	)	
	)	
Defendant.	)	

HEARING ON MOTION TO DISMISS CASE

BEFORE THE HONORABLE U.S. DISTRICT JUDGE LAURA TAYLOR SWAIN

UNITED STATES DISTRICT COURT JUDGE

APPEARANCES:

ALL PARTIES APPEARING TELEPHONICALLY

For The Commonwealth of Puerto Rico, *et al.*:	Mr. Martin J. Bienenstock, PHV
For Puerto Rico Fiscal Agency and Financial Advisory Authority:	Mr. Peter Friedman, PHV
For The Retiree Committee:	Mr. Ian Gershengorn, PHV
For The U.S. Department of Justice:	Mr. Bradley Humphreys, PHV

APPEARANCES, Continued:

For Ambac Assurance Corporation: Ms. Elizabeth Prelogar, PHV

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I N D E X

San Juan, Puerto Rico

January 12, 2021

At or about 9:56 AM

* * *

THE COURT: Good morning. This is Judge Swain speaking.

MS. NG: Good morning, Judge. It's Lisa. Everybody is here.

THE COURT: Thank you.

And, Ms. Tacoronte, would you please call the case?

COURTROOM DEPUTY: Yes, Your Honor.

The United States District Court for the District of Puerto Rico is now in session. The Honorable Laura Taylor Swain presiding.

AP case 20-6 --

THE COURT: Ms. Tacoronte, I'm having difficulty hearing you.

COURTROOM DEPUTY: I'm sorry, Your Honor. How about now?

THE COURT: That's much better. Thank you.

COURTROOM DEPUTY: Sure.

AP case --

THE COURT: And so are you going to call the caption of the adversary, also?

COURTROOM DEPUTY: Yes, Your Honor.

In re: The Financial Oversight Board of Puerto Rico, et al., Case No. 17-3283; AP Case No. 20-68, *Ambac Assurance Corporation versus the Financial Oversight and Management Board for Puerto Rico, et al.*, for hearing on motion.

THE COURT: Thank you.

And buenos dias. Welcome counsel, parties in interest, and members of the public and press. Today's hearing is for oral argument on the defendants' Motion to Dismiss the Complaint filed in Adversary Proceeding No. 20-68.

To ensure the orderly operation of today's telephonic hearing, all parties on the line must mute their phones when they are not speaking. If you are accessing these proceedings on a computer, please make sure to select "mute" on both the Court Solutions dashboard and your phone. When you need to speak, you must unmute on both the dashboard and the phone.

I remind everyone that consistent with court and judicial conference policies, and the orders that have been issued, no recording or retransmission of the hearing is permitted by any person, including but not limited to the parties, members of the public, and the press. Violations of this rule may be punished with sanctions.

I will be calling on each speaker during this hearing in the agreed order that is enumerated in the Joint Informative Motion filed at Docket Entry No. 58 on the adversary proceeding docket on January 8, 2021. When I do,

please begin your remarks by identifying yourself by name for clarity of the record.

If you wish to be heard out of order, or otherwise need to make a remark, please state your name clearly at the end of an argument segment and request to be heard. Don't just use the "wave" on the Court Solutions dashboard. Speak, I will respond to your request, and I will call on each speaker if more than one person wishes to be heard and I am granting the request.

Please do not interrupt each other or me during this hearing. If we interrupt each other, it is difficult to create an accurate transcript of the proceeding. Having said that, I apologize in advance for breaking this rule, as I may interrupt if I have questions or if you go beyond your allotted time. If anyone has difficulty hearing me or another participant, please say something right away.

The time allotments for each speaker and for each segment of the argument are set forth in the Joint Informative Motion filed in the adversary proceeding. I encourage each speaker to keep track of his or her own time. The Court will also be keeping track of the time and will alert each speaker when there are two minutes remaining with one buzz, and when time is up, with two buzzes.

Here is an example of the buzz sound.

(Sound played.)

THE COURT: If your allocation is two minutes or less, you will just hear the final two buzzes.

If we need to take a break, I will direct everyone to disconnect and to dial back in at a specified time. And the argument is scheduled to run for two hours, that is, from now until just about noon, Atlantic Standard Time.

And so I will now turn to the arguments on the motion. First, I have the Oversight Board for 25 minutes.

MR. BIENENSTOCK: Good morning, Judge Swain. My name is Martin Bienenstock, of the law firm Proskauer Rose, LLP, and we represent the Oversight Board as Title III representative of the Commonwealth.

THE COURT: Good morning, Mr. Bienenstock.

MR. BIENENSTOCK: We wish the Court, its staff, and all parties a happy, healthy new year; swift vaccinations; and look forward to returning to San Juan.

The relief the Oversight Board seeks this morning is an order dismissing Ambac's Complaint dated May 26, 2020, pursuant to the Oversight Board's Motion to Dismiss dated August 17, 2020. While we believe it is a threshold issue that Ambac is estopped on multiple grounds from participating in the Title III cases, accepting a billion dollar recovery, and three years later contending PROMESA Titles I, II, and III are unconstitutional, and demanding the Oversight Board and its members be enjoined from "any further action whatsoever in

connection with" those titles of PROMESA, I have to leave that threshold issue, because my colleague, Peter Friedman of O'Melveny, will be discussing that.

I will argue why the Uniformity Clause does not apply to PROMESA, and its application to Puerto Rico's minimum of 141 eligible Title III debtors, and why even if it does apply, based on two United States Supreme Court decisions, all relevant provisions of PROMESA satisfy the uniformity requirement.

Although the first sentence of Ambac's preliminary statement provides, "Congress enacted a private bankruptcy bill for Puerto Rico alone," Ambac shifts gears on page four of its brief and asserts PROMESA is not a local law, and on page 21, asserts it is a national law. Before I explain why Ambac is wrong, I want to point out that by arguing PROMESA is a national law and not a local law, Ambac effectively admits the Territories Clause in Article IV, Section 3 of the Constitution is not for local laws subject to the Bankruptcy Uniformity Clause in Article I, Section 8, Clause 4 of the Constitution. There is no other reason to argue the local, national distinction.

The Territories Clause uses the word "all" and is pretty clear. "Congress shall have power to dispose of and make all needful rules and regulations respecting the territory or other property belonging to the United States."

The Bankruptcy Uniformity Clause in Article I, Section 8, Clause 4 of the Constitution also clearly provides it applies to the United States, and no one contends Puerto Rico is a state. It provides, Congress shall have power to establish "uniform laws on the subject of bankruptcies throughout the United States."

On the national statute issue, Ambac's brief, at pages 21 through 28, contends Title III is a national statute. Ambac asserts two tests for whether PROMESA Title III is a local or national law. At page four of its brief, Ambac asserts, "no local law could, as PROMESA does, authorize federal courts to discharge debt held by creditors nationwide." Ambac's second test, also on page four of its brief, is whether a state legislature could enact PROMESA Title III. As I am about to show, the Supreme Court has expressly ruled to the contrary on both issues.

First I'll address the creditor location test. The Oversight Board responded to these issues on pages 11 to 16 of its Reply Brief, and I will not rehash what we said. I want to make just three points now. First, Title III is a local statute, because it only discharges debt of Puerto Rico governmental entities. And this Court, in PROMESA Section 306(b), is only granted property jurisdiction over property of the Puerto Rico Title III debtors.

Pursuant to logic and the United States Supreme Court

jurisprudence that entities outside Puerto Rico own Puerto Rico debt does not render Title III a national statute. Indeed, if Ambac's theory is correct, Title III would be an international statute, because entities outside the United States own some of its debt. Moreover, on Ambac's theory, Title III would bounce back and forth from being a local, national, and international statute, based on where the debt trades and resides any given night, even though Title III's provisions and consequences do not change.

Second, Ambac ignores the fundamental basis of bankruptcy jurisdiction. Title III is also a local statute, because it operates in rem. The significance of in rem jurisdiction is that Title III's discharge frees up only property of Puerto Rico entities and their future earning power.

Third, the Supreme Court ruled in *Central Virginia v. Katz*, 546 U.S. 356, at pages 369 and 70, that, "Bankruptcy jurisdiction, as understood today and at the time of the framing, is principally in rem jurisdiction." The Supreme Court went on to say, in bankruptcy, "the Court's jurisdiction is premised on the debtor and his estate, and not on the creditors."

In respect of Ambac's contention that the Territories Clause does not mean what it says, namely, Congress can make all needful rules and regulations, and only authorizes

Congress to enact laws a state can enact, there is no such rule. The Supreme Court has demonstrated time and again there is no such rule. And Ambac hasn't shown it would be breached by PROMESA in any event. To be clear, the Oversight Board's motion does not require a ruling that there are no constraints on the Territories Clause legislation, only that the Uniformity Clause is either not a constraint or is not violated here.

Empirically, history shows Congress enacted special debtor-creditor laws for territories. In *Hayman v. Moxley*, at the Oversight Board's Reply Brief at page ten, the Circuit Court of Appeals for the District of Columbia enforced an Act of Congress entitled, An Act for the Relief of Insolvent Debtors Within the District of Columbia. That law provided discharges.

Before getting to the Article III example, I will cover the tax cases, because Ambac supports its local law argument with a phrase from the *Binns* opinion. Article I, Section 8, Clause 1 of the Constitution contains a Uniformity Clause for taxes requiring, "all duties imposed and excises shall be uniform throughout the United States."

The Supreme Court has at least twice ruled the Tax Uniformity Clause does not apply to territories: Once in *Gibbons v. District of Columbia*, where the real property tax in the District of Columbia was one and a half percent on some

property and one and a quarter percent on other property; and once in *Binns v. United States*, that affirmed a license tax in the territory of Alaska, which was not imposed on the rest of the country.

The Supreme Court found these cases easy. For instance, in *Binns*, at page 494, the Court took as a given that "Congress has undoubtedly the power by direct legislation to impose these license taxes upon the residents of Alaska, providing that when collected, they are paid to a treasurer of the territory."

Ambac takes a snippet from *Binns* at page 12 of its brief, says, quote, Congress and the government of the territories has plenary power, save as controlled by the provisions of the Constitution. Ambac asserts that last phrase, "controlled by the provisions of the Constitution," means the Congressional power to legislate for the territory is controlled by the Uniformity Clause. But *Binns* itself shows that is not what the Supreme Court was saying.

First, the facts in *Binns*, at page 487, show it was a local statute, even though it applied to persons and corporations anywhere in the world. The tax required that any -- that "any person or persons, corporation or company, prosecuting or attempting to prosecute any of the following lines of business within the District of Alaska shall first apply for and obtain license so to do from a district court or

a subdivision thereof in said district, and pay for said license for the respective lines of business and trade as follows: To-wit, transfer companies, 50 dollars per annum." I've read it to show the tax applied to any person or corporation, which would include a person, a corporation residing anywhere in the United States, or the world.

Second, *Binns'* holding refutes Ambac, because its holding is that Congress can impose license taxes in Alaska without making them uniform across the United States. Then, at page 496, *Binns* explains exactly what being subject to the provisions of the Constitution means. *Binns* rules, "in order to avoid any misapprehension that we may add -- any misapprehension, we may add that this opinion must not be extended to any case, if one should arise, in which it is apparent that Congress is, by some special system of license taxes, seeking to obtain from a territory of the United States revenue for the benefit of the nation, as distinguished from that necessary for the support of the territorial government."

Applying that principle here, if Congress enacted a statute for Puerto Rico that restructured debt of both Puerto Rico and non-Puerto Rico entities, the statute would be subject to the Uniformity Clause, but Congress restricted PROMESA in all its titles to Puerto Rico.

Now for the Article III examples. In short, when legislating under the Territories Clause, Congress is neither

restricted by Article III's requirement of judges having lifetime tenure and irreducible compensation, nor of the requirement that admiralty jurisdiction be reserved to the Federal Courts.

The *American Insurance Company* decision cited in the Oversight Board's opening and reply briefs provides, at page 546, quote, although admiralty jurisdiction can be exercised in the states in those courts only which are established in pursuance of the third Article of the Constitution, the same limitation does not extend to the territories. In legislating for them, Congress exercises the combined powers of the general and of the state government. Thus, Ambac's state government only rule was disproved 127 years ago. And, Judge, it gets better with age.

In its seminal *Northern Pipeline* decision, the Supreme Court quoted and adopted that same language and more. The Supreme Court, in its *Northern Pipeline* decision, 458 U.S. 50, shows Ambac is wrong in two ways: First, the Supreme Court comes right out and rules Congress' legislation under the Territories Clause is an exception to Article III. Second, the Supreme Court rules Congress' power of government over the territories is "complete."

Here's what *Northern Pipeline* says at pages 64 and 65. Appellants first rely upon a series of cases in which this Court has upheld the creation by Congress of non-Article

III territorial courts. This exception from the general prescription of Article III dates from the earliest days of the Republic when it was perceived that the framers intended that, as to certain geographical areas in which no state operated as sovereign, Congress was to exercise the general powers of government.

For example, in *American Insurance Company v. Canter*, the Court observed that Article IV bestowed upon Congress alone a complete power of government over territories not within the states that constituted the United States. The Court then acknowledged Congress' authority to create courts for those territories that were not in conformity with Article III. Such courts were -- and then skipping a few lines, the *Northern Pipeline* decision says, although admiralty jurisdiction can be exercised in the states in those courts only which are established in pursuance of the third Article of the Constitution, the same limitation does not extend to the territories. In legislating for them, Congress exercises the combined powers of the general and of the state government.

The Court followed the same reasoning when it reviewed Congress' creation of non-Article III courts in the District of Columbia. It noted that there was in the district no division of powers between the general and state governments. Congress has the entire control over the

district for every purpose of government, and it is reasonable to suppose that, in organizing a judicial department here, all judicial power necessary for the purposes of government would be vested in the courts of justice.

Although *Northern Pipeline* was a plurality holding, *American Insurance* was a majority and had no dissent. Additionally, the Supreme Court has approved *Northern Pipeline,* and has followed its holding several times, for instance, in *Stern v. Marshall*, 564 U.S. 462, at pages 484, 487, 493, 494 and 495.

Finally, nowhere does Ambac explain why this Court should assume the framers of the Constitution were so narrow-minded that they assumed a United States bankruptcy law could apply to every property law and debtor-creditor regimen anywhere the United States might acquire a territory in the rest of the world. For instance, in Canada and other jurisdictions, they have a debtor-creditor concept called a floating charge. It's not easy to categorize it as a secured claim or unsecured claim. The U.S. Bankruptcy Code imposes interest requirements. Some parts of the world do not allow interest. And so on.

While the Oversight Board submits that even if there is a uniformity requirement, Title III does not need to be uniform with Chapter Nine, it is anyway, because the Supreme Court's *Blanchette* decision shows the existence of an

authority that formulates and even makes determinations about the reorganization plan, does not render a bankruptcy regime nonuniform from regimes not having such an authority.

In short, Ambac's arguments that Title III is nonuniform with Chapters 9 and 11 are soundly refuted by the Supreme Court decisions Ambac cites. First, history and logic have a lot to say here. Since Congress enacted its first bankruptcy legislation in 1800, Congress has enacted different bankruptcy laws for individuals liquidating their assets, individuals with regular income desiring a payment plan, individuals and entities desiring to reorganize, farmers, railroads, single asset debtors, small businesses, municipalities, commodity brokers, stockbrokers, clearing banks, and debtors subject to foreign proceedings.

All those different regimens are in Title 11 of the United States Code, and broker dealers are eligible for bankruptcy under the Securities Investor Protection Act of 1970. It cannot be that a bankruptcy regimen for a territory and its instrumentalities must be uniform with all those regimens, and if it must be uniform, which regimen must it be uniform with. It can't be uniform with all of them.

Ambac takes Chapter Nine as the standard, and that has initial and superficial appeal, because Chapter Nine is for governmental units, albeit not territories. But its appeal is only superficial, because Chapter Nine was

constructed to avoid violating the 10th Amendment. That is why there is no provision for an oversight board or trustee.

Precisely because territories are not within the 10th Amendment, PROMESA imposes an oversight board with numerous powers incompatible with the Tenth Amendment. Thus, Ambac's position defies the Supreme Court's teaching in *Blanchette* that, quote -- this is 419 U.S., at 159 -- the uniformity provision does not deny Congress power to take into account differences that exist between different parts of the country, when -- to fashion legislation to resolve geographically isolated problems. We, therefore, agree with the special court that the Uniformity Clause was not intended to hobble Congress by forcing it into nationwide enactments to deal with conditions calling for remedy only in certain regions.

Ambac does not recognize Congress' power to deal with special and unique problems, rather, it rides two horses: On one horse, it tries mightily to shoehorn Puerto Rico, with its 141 eligible governmental debtors, into the *Gibbons* case, striking down a private bankruptcy bill for one debtor and one court. On the other horse, Ambac packs its contentions about lack of uniformity, which generally fall into two batches. In one batch, Ambac complains about provisions it contends allow the Oversight Board -- or cause the Oversight Board to believe it can pick winners and losers. In the second batch, Ambac points to a Title III provision providing the Oversight Board

the power to limit the amount of debt issued under a Title III plan of adjustment by its debt sustainability analysis in its certified fiscal plan, although the Court is not required to confirm any plan the Oversight Board proposes.

As far as there being nonuniform provisions allowing the Oversight Board to pick winners and losers, PROMESA Section 301(a) shows indisputably that the same unfair discrimination provision in Chapters 9 and 11 is in Title III, along with a host of other identical provisions.

I want to focus on Ambac's contention that PROMESA Section 314(b)(7) renders Title III nonuniform with Chapters 9 and 11. It provides as conditions confirmation that, "the plan is consistent with the applicable fiscal plan certified by the Oversight Board under Title II."

Ambac's contention is demonstrably wrong. Ambac doesn't mention that the Supreme Court has already rejected such an argument in the context of one of its main authorities, *Blanchette v. Connecticut General Insurance Corporations*, 419 U.S. 102, at page 163. There, Justice Douglas in dissent argued Ambac's argument. Justice Douglas argued that, because Section 77 reorganization's required under Section 77(d), the Interstate Commerce Commission define the plan as fair and equitable before it can be confirmed, but the Rail Act did not require the Interstate Commerce Commission -- I'm sorry. That the Rail Act did not

require the Interstate Commerce Commission to make such finding. The Rail Act provisions for railroads in the Midwest were not uniform with Section 77 Railroad Reorganization provisions.

The ICC had more power than the Oversight Board in that its word was final on valuation and many other fact issues. Parenthetically, in response to Ambac's complaint that the Oversight Board represents each Title III debtor even when they have claims against one another, the ICC controlled in Section 77 reorganization plans of every railroad, whether competitors or not. Section 77(b) provided, "no plan shall be approved or confirmed by the judge in any proceeding under this section unless the plan shall first have been approved by the commission and certified to the Court."

Justice Douglas' dissent in *Blanchette* also cites *Ecker v. Western P.R. Corp.*, 318 U.S. 448, and specifically pages 472 to 476, which shows how many more powers the Interstate Commerce Commission had over Section 77 railroad reorganizations than the Oversight Board has over a Title III plan of adjustment. But the Supreme Court rejected the contention that these powers that the ICC had over the Court rendered Section 77 nonuniform to the Rail Act. The ICC not only had to approve the plan, it also made key unreviewable findings about it. The ICC determined valuation, which directly controlled which of the creditor's claims and

shareholder's interests could participate in the reorganization value.

Ecker ruled, quote, the power of the Court does not extend to participation in all responsibilities of the commission. Valuation is a function limited to the Commission, without the necessity of approval by the Court. The first sentence of the last paragraph of (e) provides, if it shall be necessary to determine the value of any property for any purpose under this section, the Commission shall determine such value and certify the same to the Court in its report on the plan.

The *Ecker* Court goes on to talk about the ICC's power over the public interest, determining whether the plan was in the public interest, the formulation of the classification, and other key issues to any reorganization plan. The Court in *Ecker* said leaving the problems of public interest to the Commission was not a departure from precedent. The phrase had been employed long before in the grant of authority to supervise the issue of securities.

The Court went on to say, the development of the capitalization of the reorganized company, which is entrusted solely to the Commission under the requirement that the plan be compatible with the public interest, is that relating to the total amount of issuable securities and the quality of the securities to be issued. So long as legal standard is

followed --

(Sound played.)

MR. BIENENSTOCK: -- the judgment of the Commission on such capitalization is final.

Ambac's shoehorning into *Gibbons* just doesn't work. Puerto Rico is not one debtor. It's 63 initially covered entities, plus 78 municipalities, for 141. Currently, there are six Title III cases pending. They could not be more different: Different creditors, different issues, different governmental functions, different outcomes, COFINA, Commonwealth, PREPA, HTA. Your Honor understands.

THE COURT: Yes.

MR. BIENENSTOCK: Ambac's position destroys the policies to be served by Title III by defying the Supreme Court's teaching that Congress can address geographically unique problems. As this Court knows, PROMESA is strong medicine. It causes Congress to create an Oversight Board with lots of powers over the territorial government. The Commonwealth Government's strong opposition to those powers has punctuated plenty of litigation in this Court.

While Ambac attempts to show the Virgin Islands was over leveraged and shut out of the debt markets, Ambac hasn't alleged and provided a scintilla of evidence showing the Virgin Islands want that medicine or have asked for it. That is critical for a very important reason. The lesson here is

that the appointment of an oversight board is what prevents Title III from being a moral hazard in which governments run up debt out of control on the theory they can discharge it in Title III. The loss of important governmental and political powers to an oversight board is what deters territory governments from both irresponsibly incurring debt and failing to try to deal with their own debt by imposing measures to restore fiscal responsibility. Ambac's position, however, destroys all that.

According to Ambac, Title III either needs to eliminate the Oversight Board to make it uniform, or all territories need the appointment of an oversight board immediately. Ambac's first alternative eliminates --

(Sound played.)

MR. BIENENSTOCK: May I just finish the sentence, Your Honor?

THE COURT: Yes, you may.

MR. BIENENSTOCK: Thanks.

Ambac's first alternative eliminates the only component of PROMESA designed to restore fiscal responsibility and market access, while Ambac's second alternative indiscriminately usurps local government power from all territories that have been fiscally responsible.

THE COURT: Thank you, Mr. Bienenstock.

MR. BIENENSTOCK: Your Honor, subject to the Court's

questions, I would end here, subject to the rebuttal time.

THE COURT: Yes. Thank you. You've been quite comprehensive in your remarks, and so I don't have questions for you at this point.

We will turn to AAFAF, which has been allotted six minutes.

MR. FRIEDMAN: Good morning, Your Honor. Happy new year. Peter Friedman of O'Melveny & Myers. I'm going to discuss estoppel and laches.

So I think one of the keys to understand -- if you look at Ambac's Complaint, which makes clear that it's about the statute as written, not about as applied, if you look at the chart in their Complaint on page 47, every single allegation and provision of PROMESA that they allege is nonuniform is clearly identified and is knowable. And if you look at its Complaint at paragraphs 68 to 73, in their own words they say the differences have affected the entire Title III case.

So they knew about this years ago. And they knew when they talk about various issues, like the Commonwealth and the Oversight Board's refusal to pay special revenues over to them, which has been clear from the very beginning of the case. And they knew, when they talk about fiscal plans, which were promulgated even -- that had no room for debt service, which were promulgated even before the Title III case was

initiated. They knew, and that knowledge is one of three interlocking strands joined together to bar the Complaint, because knowledge we understand is the benefit they received. And together, those three aggregate to constitutional estoppel, judicial estoppel, and the application of laches.

With respect to constitutional estoppel, this Complaint came three years into the Title III cases. And we've cited numerous cases that say when you receive a benefit under a statute, you cannot subsequently turn around and challenge the constitutionality of that statute. And Ambac's response boils down to, well, we didn't really receive a benefit in respect to COFINA, because we just participated. But that's not true, and we know it's not true for several reasons.

We know it's not true, as we pointed out, because the Confirmation Order says that Ambac and other parties received special fees on account of their efforts in assisting with the formulation of the COFINA Plan. We know that Ambac touted the COFINA Plan in connection with various public statements its made. We know because Ambac signed the PSA. And in Sections 4.6(c) and (f), Ambac didn't just simply sit by passively with the PSA, but it agreed to support the COFINA Plan, to support the COFINA Disclosure Statement, and even in 4.6(f), it agreed to support the Commonwealth-COFINA settlement in the Commonwealth Title III case.

To put it -- to be any plainer, they received substantial benefits, and they are nothing like the school child who had to pay an extra fee in the *Kadrmas* case to ride across in a bus, across the tundras of North Dakota to get to school. That is not Ambac, and that's a completely different situation.

The *Kadrmas* case, which they cite to say means that if you just sit by and do the bare necessities, you can't be constitutionally estopped, there is no resemblance to this situation. And neither did the *Abie* case which they cite to say that they didn't receive a meaningful benefit, because there is somebody waiting for years to bring suit. And of course the difference they overlook in the *Abie* case is that the *Abie* plaintiff lost immediately when they tried to challenge the statute, and that the Court held it wasn't constitutionally estopped was a subsequent challenge many years later.

With respect to judicial estoppel, it's good to remember just about exactly two years ago today when we were all in person, Ambac came to the Court and said that the Court could pass on a COFINA new bond legislation precisely because PROMESA was different than Chapter Nine.

(Sound played.)

MR. FRIEDMAN: That argument helped fill a void that -- the Court had pointed out that it wasn't clear it had the

authority to do certain things. Ambac stepped into that void to say the differences between the two statutes were important and meaningful, and I think the Court relied on that. And it's precisely the kind of fast and loose behavior that we see applications estopped.

With respect to laches, again, we know this case has gone on for more than three years. We know that rights have been determined, contracts have been rejected, hundreds of millions of dollars have been spent, and Ambac didn't bring its facial challenge to this statute. And Ambac's response is, well, we were trying to work things out or consensually negotiate and, therefore, we weren't obligated to bring suit immediately.

Your Honor, the ECF is littered with receipts that just demolish that argument. Ambac has relentlessly pursued lawsuits arguing the unfit constitutionality of various behaviors by the Commonwealth and AAFAF. So it's just simply not credible to argue that they were sitting and trying to resolve things consensually while, at the same time, pursuing suits arguing a whole variety of constitutional infirmities in the Title III cases and fiscal plans.

Your Honor, the last issue I want to address is the issue of whether you can grant -- well, you can hold laches is inapplicable as a defense to prospective relief. And what I would say is that it fails at the inception. This isn't

prospective relief. This would destroy an ongoing project. As I said, there are contracts that have been rejected; rights have been determined; funds have already been expended. Cases would potentially have to be dismissed if the Court were to enter the relief. Not even potentially. Would undoubtedly have to be granted. A motion to dismiss the case would undoubtedly have to be granted if this Ambac request is granted.

(Sound played.)

MR. FRIEDMAN: And that's not simply prospective relief.

Unless the Court has any questions, I reserve the remainder of my time for rebuttal, Your Honor.

THE COURT: Thank you, Mr. Friedman.

Next I have the Retiree Committee for three minutes.

MR. GERSHENGORN: Thank you, Your Honor. May it please the Court, Ian Gershengorn from Jenner & Block.

I want to make three principal points in my time this morning. First, the uniformity provision of the Bankruptcy Clause in Article I does not apply when Congress enacts a local, debt-related law under Article IV. Mr. Bienenstock made the textual points, and I won't repeat them, but I want to add that the textual reading makes good sense.

Article I contains careful limits on Congressional power, because sovereign states demanded uniform treatment in

return for relinquishing their sovereignty to the Federal Government. By contrast, the Territories Clause is an expressed disuniformity provision. Article IV allows Congress to make all needful rules and regulations for the territories, and to act in ways, as the Supreme Court has said, that would exceed its powers or at least be very unusual in other contexts.

Ambac says that this Court should ignore all this and apply a functional analysis, but it's the text that governs. And as a textual matter, any uniformity requirement is a limit on Congress' Article I power, not its Article IV powers. Regardless, Ambac gets the functionality analysis wrong, because it ignores the function of Article IV.

The framers gave Congress a broad latitude --

(Sound played.)

MR. GERSHENGORN: -- to develop innovative approaches to territorial government, consistent with the need for inventive statesmanship in the territories. It, thus, would be wrong as a functional matter to apply a uniformity straitjacket to local territorial legislation.

My second point this morning is that this is local legislation. How do you know that? The Supreme Court in *Aurelius* said so. The Court said Congress exercised its power under Article IV to, quote, make local, debt-related law, and that PROMESA creates a process for determining, quote, certain

local policies related to local fiscal responsibility in respect to local matters.

Ambac makes two principal counter arguments: First, it argues that PROMESA can't be local, because it supposedly has nationwide effect, but that's the precise argument that *Aurelius* made and the Supreme Court rejected. Second, Ambac argues that PROMESA is not local, because a local legislature could not have passed it, but no case requires that Congress' Article IV power be viewed through the prism of what a hypothetical local legislature could or could not do.

When Congress acts in the territories, Congress has, quote, full and complete legislative authority over the people of the territory. The right question under *Binns* is not what a local legislature could do, but rather whether Congress acted to benefit a territory, rather than the nation.

Finally, Your Honor, I want to just say a word about why PROMESA is constitutional, even if the Uniformity Clause applies. Ambac relies on *Gibbons*, but the bottom line is that Puerto Rico is fundamentally different from a single railroad. It's a sovereign government, not a private corporation. And it has a responsibility for providing essential government services to three million people, and those services were at risk.

In *Blanchette*, the Supreme Court said the Uniformity Clause was not intended to hobble Congress by forcing it into

nationwide enactments to deal with conditions calling for a remedy only in certain regions. If *Blanchette* means anything at all, it means that Congress can pass PROMESA to address the fiscal sovereignty of Puerto Rico and to protect the health of its residents.

(Sound played.)

MR. GERSHENGORN: If the Court has no questions, I'll save the remainder of the time for rebuttal.

THE COURT: Thank you, Mr. Gershengorn.

And now, for the United States, I have an allocation of eight minutes.

Mr. Humphreys, would you unmute yourself on the dashboard and on your phone?

MR. HUMPHREYS: I apologize. It's my first time, Your Honor. I'm now unmuted on both.

THE COURT: Thank you.

MR. HUMPHREYS: Good morning, Your Honor.

THE COURT: Good morning, Mr. Humphreys.

MR. HUMPHREYS: Happy new year. Thank you.

THE COURT: Happy new year.

MR. HUMPHREYS: Brad Humphreys of the United States Department of Justice on behalf of the United States.

The question of whether PROMESA violates the uniformity provision in Article I, Section 8, does not present a closed question, and accepting Ambac's arguments would

require the Court to disregard decades of precedent interpreting Article I's uniformity provisions. As the Court is well aware, Congress enacted PROMESA pursuant to its authority in Article IV, which authorizes Congress to make all needful rules and regulations respecting a territory.

As the Supreme Court recently reiterated in *Aurelius*, Article IV gives Congress the power to legislate for the territories in ways that it would not be able to, or at least would be very unusual in other contexts. And similarly, as Mr. Gershengorn just pointed out, the Supreme Court has said that Article IV gives Congress broad latitude to develop innovative approaches to territorial governments. And that's from the Supreme Court's decision in *Puerto Rico v. Sanchez Valle*.

In PROMESA, Congress looked to the unique circumstances facing the people and Government of Puerto Rico caused by the debt crisis in 2016, and developed a local, debt-related law based on those particular circumstances. Ambac, of course, claims that Congress was limited by the uniformity requirement in Article I, Section 8, of the Bankruptcy Clause specifically; but as the government explained in its briefs, that limitation applies only when Congress exercises its Article I enumerated powers, not when it's legislating for territories under Article IV. And Ambac lacks a convincing argument why a limitation on Congress'

Article I powers would apply when it's actually exercising its Article IV authority as local, debt-related law, as the Court recognized in *Aurelius*, particularly in light of the Supreme Court's decision in *Binns*, which Mr. Bienenstock discussed at length.

That a uniformity requirement does not apply is also clear from the specific language of the provision, which requires uniformity only throughout the United States. That limitation has been interpreted, with respect to the taxation uniformity requirement, to exclude Puerto Rico explicitly. Moreover, accepting Ambac's contrary argument would create significant tension with the Supreme Court's decision in *Puerto Rico v. Franklin California Tax-Free Trust*, which held that Puerto Rico is not a state for the purposes of the Bankruptcy Code's gateway provision, and that Puerto Rico's municipalities, therefore, could not avail themselves of the Chapter Nine reorganization.

If the uniformity requirement, in fact, applied to Puerto Rico, then there could potentially be a conflict and create a uniformity issue in the Bankruptcy Code itself, potentially going back to the 1930s. And nothing in the *Franklin* case suggests, however, that there is such a problem. It's simply implausible, in light of *Franklin,* to believe that Congress has treated Puerto Rico differently for many decades if the uniformity requirement is as stringent as Ambac

asserts.

I'd also note that the Supreme Court cited the uniformity requirement when deciding *Franklin*, and there was a concurrence addressing the issue at length in the Circuit Court decision. So it's not as if the Supreme Court were not aware of the Article I, Section 8, requirement when it decided the case.

Applying the uniformity requirement and the Bankruptcy Clause to Puerto Rico would also be inconsistent with how courts have interpreted other uniformity requirements in Article I. The courts have long interpreted the uniformity requirement for naturalization, which is contained in the same sentence of Article I, Section 8, to allow Congress to set different rules among the territories. Specifically, I'd point the Court to the Ninth Circuit's decision in *Eche*, where the Court concluded that the uniformity requirement did not prevent Congress from treating differently citizens from the Commonwealth, the Northern Mariana islands. And, of course, Congress has long set different rules for naturalization of residents in different territories, as we discussed in our brief.

Furthermore, as to the Taxation Clause in Article I, Section 8, which also includes a uniformity requirement, the Court in *Binns*, of course, upheld taxes that applied only to the *Binns*' -- territory of Alaska. It's also telling that

residents of Puerto Rico at present are taxed differently in some ways than residents in the 50 states, in a way that is beneficial to residents of Puerto Rico. And those differences could arguably be unlawful if the uniformity requirements for taxation in Article I, Section 8, were as stringent as Ambac claims.

Ambac asks the Court to ignore all of this, the structure, text, other cases interpreting uniformity requirements, and to conduct a so-called functional analysis to decide whether the uniformity requirement and the Bankruptcy Clause applies to the territories. However, the Supreme Court in *Blanchette* and *Ptasynski* has instructed that the Uniformity Clause should be interpreted consistently with each other. So the Court should not simply ignore those cases in the context of taxation and naturalization in favor of a free-floating outcome driven test like Ambac advances.

Indeed, the government submits that it would defy core principles of interpretation to say that uniformity in one clause means something completely different when used in a different clause in the same section. Because the Bankruptcy Clause's uniformity provision does not apply, Ambac's challenge to PROMESA fails.

However, even if the Court could get past that threshold issue, which we don't think is possible, PROMESA would still be constitutional if the uniformity requirement

were to apply. That requirement in the Bankruptcy Clause is inherently flexible and allows Congress to pass legislation to solve geographically isolated problems.

Indeed, the Supreme Court has invalidated a law as inconsistent with the Bankruptcy Clause only once, in *Gibbons*, where it concluded that Congress had --

(Sound played.)

MR. HUMPHREYS: -- effectively created a private bankruptcy law. Even in *Gibbons*, however, the Court emphasized that the uniformity requirement is not a straitjacket that forbids Congress from distinguishing among classes of debtors.

And, of course, the Supreme Court upheld the bankruptcy statute that was limited to a specific region in *Blanchette*, explaining that the uniformity provision does not deny Congress to take into account differences that exist in different parts of the country, and to fashion legislation to solve geographically isolated problems. There can be no serious question that that's exactly what Congress did in PROMESA.

In 2016, Puerto Rico faced a crushing public debt crisis, and had lost access to credit markets, and it had lost the ability to provide its citizens with effective services. In other words, the evil to be remedied, the statute, was Puerto Rico's local public debt crisis. So it was within

Congress' power to design a solution to address that problem without violating the Uniformity Clause, and the Court need only look to *Blanchette*.

And as the Supreme Court indicated in *Ptasynski*, even where Congress has drawn distinctions based on geography, courts should be reluctant to disturb Congress' judgment with respect to enormously complex problems just like this.

If the Court has no further questions, I will conclude my remarks.

THE COURT: Thank you, Mr. Humphreys.

MR. HUMPHREYS: Thank you, Your Honor.

THE COURT: I now have an allocation of 60 minutes for argument on behalf of Ambac. Who is speaking first?

MS. PRELOGAR: Yes. Good morning, Your Honor. This is Elizabeth Prelogar from Cooley representing Ambac.

THE COURT: Good morning, Ms. Prelogar.

MS. PRELOGAR: Your Honor, good morning.

This case raises a critically important question under the Constitution of whether Congress may permissibly single out one territory, Puerto Rico, and create for it a unique bankruptcy process that differs from all other debt restructuring proceedings, whether compared to other territories, compared to other governmental entities, or compared to any other conceivable class of debtors. PROMESA violates the bankruptcy uniformity requirement and the

Constitution, and the Motion to Dismiss should be denied.

The parties on the other side have made a number of claims in defense of PROMESA, both at the hearing today and in their briefs, that really fall into four main categories: About whether the bankruptcy uniformity requirement applies in the territory; whether PROMESA can qualify as a uniform law; whether the constitutional violation here could be fixed by extending PROMESA; and then a number of procedural objections. And I want to make sure to respond to each of those issues, but I'll take them in order and begin with the threshold question of whether PROMESA is subject to the uniformity requirement in the first place.

The Oversight Board's theory here is that because Congress invoked its Article IV powers when it enacted PROMESA, all other constitutional constraints and limitations on Congress' authority are inapplicable. Essentially, this is an argument that the Constitution just doesn't apply when Congress takes action related to the territories, and that categorical claim is inconsistent with precedent. Most notably --

THE COURT: Ms. Prelogar, there's maybe a bit of an overstatement. They're saying that the Constitution applies. They're citing Article IV of the Constitution, but they're saying that Article I does not govern Article IV.

So I realize that one has to be aggressive in one's

argument, but please be as precise as you can be.

MS. PRELOGAR: Absolutely, Your Honor. And it's absolutely the case that they've argued that, when Congress here relies on Article IV, that's the source of authority; but the important thing to recognize is that would effectively make the invocation of Article IV authority an on-off switch for any other restrictions in the Constitution. But so long as Congress is taking action related to the territories, so long as it's making needful rules and regulations with respect to the territories, it's not necessary to look at other constraints in the Constitution. And we think that that's at odds with Supreme Court precedent.

Most notably and most recently, it conflicts with the Supreme Court's decision just last term in the *Aurelius* case -- of course, Your Honor's familiar with that -- involving PROMESA itself and the Appointments Clause challenge. And I do want to pause on *Aurelius* for a minute and walk through it, because I think that it refutes the suggestion that the Oversight Board has made here that any law enacted pursuant to Article IV qualifies as a local law.

So the Oversight Board has made clear in its Reply Brief that it's using these terms, local law, national law, to refer to Article IV exercises of authority, which is Article I. And the Oversight Board has contended that so long as it's an Article IV statute, or that was the source of authority

that Congress invoked, automatically it qualifies as a local law. But if that were right -- the Supreme Court of course recognized in *Aurelius* that Congress had invoked Article IV to pass PROMESA, and that could have been the end of the Court's analysis. In the Oversight Board's view, the Court could have just stopped there and said, okay, it's an Article IV statute; therefore, it's a local law, and it's not necessary to consider then whether the Appointments Clause would operate as some kind of restriction or restraint on what Congress has done. But that's not what the Supreme Court did.

The Court went on to consider the purpose of the Appointments Clause and emphasize that that purpose is to ensure political accountability, and ran through the text and the history of the clause. And it was specifically noted that many times Congress had complied with the Appointments Clause in appointing officers of the United States who were exercising power in the territory.

So, ultimately, the Court in *Aurelius* concluded that Congress can be bound by the Appointments Clause when it creates officers of the United States, even if it's acting pursuant to Article IV, and even if those officers are exercising power in or in relation to the territories.

Now, Mr. Gershengorn this morning and the parties generally have emphasized the second holding in *Aurelius*. This was the holding, of course, that the Board members are

local officers. But there the Supreme Court was considering the classification of the Board members themselves. It wasn't considering the classification of PROMESA. And the holding with respect to the Oversight Board members turned on the fact that they were exercising primarily local duties in these proceedings. In fact, the Court emphasized that the Oversight Board members were, effectively, like any state or local officials, to supervise bankruptcy proceedings under Chapter Nine.

That doesn't mean that PROMESA is a local law any more than Chapter Nine would be a local law just because state and local officers supervise the bankruptcy proceedings on behalf of the debtor. So we do think that *Aurelius* itself forecloses this idea that PROMESA automatically qualifies as a local law just because of the invocation of Article IV authority, or just because of the fact that Congress is taking action that's related to a territory.

The central precedent that the Oversight Board has relied on, and it's come up in several of the presentations this morning, is *Binns versus United States*. But we actually think that this proves the point and shows the distinction between what truly qualifies as a local law passed by Congress with respect to a territory, that is, Congress stepping into the shoes of what a state legislature could do, versus Congress having to rely on its unique federal authority in

order to pass a statute.

And so maybe I could just walk through the facts of *Binns* for a moment. *Binns* involved a tax for Alaska when Alaska was still a territory. At that point, Alaska didn't have its own legislature, and so there was no other entity that could have passed any kind of tax to pay for territorial government. What the Supreme Court said is that Congress has the power to levy taxes, and here I'm going to quote, in like manner, as the legislature of a state may tax the people of a state for state purposes.

This is the kind of reasoning the Court has frequently employed in this context. *Cincinnati Soap* is another example, where the Court said Congress has, quote, equivalent power of a state in comparable circumstances. And, again, this is based on the practical consideration that there might not be another entity that's available to create the structures of local government for a territory to pass local legislation, particularly if, as in Alaska, there was no territorial legislature, and so an exercise in this local authority.

And this explains the language about Congress being able to act in ways that are unusual. The Court has emphasized that Congress can essentially act as a state or municipality may act, and it's not bound by the same constitutional restrictions that, for example, create the

structures of the Federal Government. But the key limitation that was recognized in *Binns* and in other cases is that Congress must be doing what a state or locality could do.

And we think that the final paragraph of *Binns* makes this point perfectly clear, because that was the point in the decision where the Supreme Court said that if Congress had instead passed the tax for the benefit of the nation, and so it was doing something that no state or locality could do, the analysis would be different. In that respect, Congress would be exercising authority at the national legislature, and so could be subject to these other constitutional constraints, even though it would still be applying that tax in the territory.

In its Reply Brief, the Oversight Board asserts and emphasizes that the tax in *Binns* was paid into the national Treasury. And they say, well, no state could do that, collect a tax and pay it to the national Treasury, but of course no state could have the members of Congress pass a law for it either. These are little procedural details. They don't go to the substance of the law and the question of whether that substance is something that falls within the domain of a state and local jurisdiction.

In *Binns*, the Supreme Court deemed it critical that the funds that went into the Treasury also came out of the Treasury to pay for the governance of the territory. So this

is really equivalent to what any state could do in collecting a tax and then using that tax to pay for the structures of the state government. And that was a critical element of the Court's analysis in recognizing that Congress could lawfully impose that tax in Alaska, just as a state could.

So with respect to this local law issue, the relevant inquiry becomes, could a state or local government pass a law like PROMESA. And the answer to that is clearly no. No one on the other side is really arguing differently. It's acknowledged by the Oversight Board that principles of preemption, and of course the Contracts Clause, would mean that no state could create this kind of nationwide scheme for the discharge of debt.

And, of course, this Court need look no further than to what Puerto Rico actually did when it tried to pass its own debt restructuring scheme. But Puerto Rico took this approach in the Debt Recovery Act, and it was invalidated by the Supreme Court in the *Franklin California Tax-Free Trust* case. So that demonstrates and further confirms that this isn't the kind of local law that would fall within the subject matter or domain of any state or locality, and that makes sense.

PROMESA is a national bankruptcy law. The statute restructures debt. It provides a mechanism for this Article III court to exercise nationwide jurisdiction and order the discharge of debt held by creditors nationwide, not just

confined to Puerto Rico. Those judgments are entitled to full faith and credit. And so this looks nothing like the kind of law that any state or local government could pass in the exercise of its police powers or in otherwise attempting to manage its local affairs. And for that reason, PROMESA necessarily depends on Congress' federal authority in this regard to have that capacity and authority to pass national bankruptcy law. So that's an authority that's been recognized to be circumscribed by the uniformity requirement.

I want to respond for a moment to the points that Mr. Gershengorn and Mr. Humphreys raised about whether the analysis turns on whether Congress invoked Article I or whether it invoked Article IV, but for purposes of analyzing bankruptcy uniformity, that distinction doesn't matter. And we think that is perfectly clear from the analysis of the Supreme Court in *Gibbons*, where the United States made the same type of argument that there was another source of Congress' authority to pass the statute there, specifically, the Commerce Clause.

And so the United States said, because there was that Commerce Clause authority, it wasn't necessary to look at the Bankruptcy Clause at all or to apply the bankruptcy uniformity requirement. So what *Gibbons* said is it doesn't matter if there are multiple sources of authority to enact the law. The relevant question is, does this law touch on the subject of

bankruptcy. In other words, is it a law that's addressed to the relations of a debtor and its creditors? Is it a law that orders the discharge of debt? If so, then it's a bankruptcy law, and Congress can't avoid application of the uniformity requirement by suggesting that there's actually some other source of law that exists that fully justifies the action it took.

So we think that the distinction here between "person" in Article I and Article IV is beside the point. The relevant question is, is PROMESA a bankruptcy law. And the answer is yes.

I want to emphasize as well, though, that rather than applying any bright-line rule about whether PROMESA is subject to the uniformity requirement, the right approach here is to follow the functional analysis. This is the Supreme Court's test, and it's the way that it has approached these various questions about whether different constitutional provisions apply in the territories.

And there was a statement in the Reply Brief that questions where this test comes from or asked what the grounding was. The answer is this comes straight from the Supreme Court. That was the language, in fact, that the Supreme Court used in the *Boumediene* case. There the Court specifically said that it was applying a functional approach, and the Court summarized and traced the Supreme Court's

decisions in this area, looking at a wide variety of different constitutional provisions to determine whether those provisions did or did not apply in the territory.

So the idea that --

THE COURT: Pardon me, Ms. Prelogar. *Boumediene*, again, was looking at the question of sovereignty, correct?

MS. PRELOGAR: It was looking at the question of whether the Suspension Clause applied extraterritorially, outside the United States.

THE COURT: Yes. And that related to whether the geographical area involved was actually de facto or de jure under the sovereignty of the United States?

MS. PRELOGAR: Yes. That was one of the issues in *Boumediene*, but it relied --

THE COURT: And that's the context in which the functional language came up as I recall.

MS. PRELOGAR: Yes. But I think what's clear is that in articulating that test, what the *Boumediene* court did is it looked at a number of precedents involving the territories; and specifically analyzed the approach the Court had taken in prior cases about whether constitutional provisions had applied; and specifically discussed a number of the cases that we've been discussing here this morning with respect to the same questions of purpose of constitutional provisions, the same questions of the practical effect of extending these

provisions to the territories.

And I should emphasize, of course, that there are a number of additional cases that consider these same types of issues, about whether particular provisions in the Constitution extend to the territories, in a number of contexts. The Court has looked at the Commerce Clause. It's looked at, for example, the prohibition on passing ex post facto laws and bills of attainder. Various provisions of the Bill of Rights have been recognized to apply to the territory, and so would constrain Congress' action. That includes the First Amendment, the Fourth Amendment, the Eighth Amendment.

And so I think that what this analysis demonstrates is that when Congress is taking action with respect to a territory, in each instance it's necessary to look at a particular constitutional provision and evaluate it on its own terms. That, in fact, explains the Article III examples that Mr. Bienenstock had cited this morning.

I want to pause for a moment on the *American Insurance Company versus 356 Bales of Cotton* case. We think that that case is consistent with the pragmatic functional approach that the Supreme Court has taken in looking at whether particular constitutional provisions apply in the territories. So that was a case where the Congress had created territorial courts. It was in Florida, when Florida was still a territory. And the Supreme Court emphasized

there, and its analysis is repeated in any number of cases, that Congress has to have the power to structure territorial government. It has to have the power to create court systems, to create territorial legislatures, to delegate certain responsibilities to those territorial legislatures.

And in doing so, as a practical matter, and as a part of this functional approach, the Court has recognized that there are practical reasons not to give life tenure to territorial judges. For example, Florida later became a state. What would have become of the life-tenured municipal judges if, in fact, that Article III restriction had applied?

So there were practical reasons not to extend the Article III life tenure requirement to the territorial court. There were also practical reasons to ensure that the territorial courts could exercise admiralty jurisdiction, and that's because there were no federal courts operating side by side in Florida that could have exercised that jurisdiction. There it was a salvage claim. And so the concern was that the territorial government simply couldn't have functioned if there were particular types of claims, like salvage claims, that couldn't be heard in the territorial court.

None of this analysis suggests that Congress is just free from all constitutional constraints when it invokes Article IV. We think these cases just show that Congress wasn't required to follow that particular Article III

constraint in creating territorial courts for practical reasons.

And I'll emphasize as well that there's no explanation on the other side for why bankruptcy uniformity should not apply in the territories, looking again at the purpose of the constitutional provision, whether the purpose would be advanced by applying the law in the territories, and further looking at whether there would be any practical obstacles.

The purpose of the uniformity requirement, and this comes from cases like *Gibbons*, is to essentially prevent discrimination against creditors and thereby protect national commerce. So the time of a binding -- there were a wide variety of state discharge schemes in bankruptcy. There was a wide variation, and, in particular, a lot of discrimination against out-of-state creditors, against British creditors. And so the framers thought that Congress should have this power to create a unique -- I'm sorry, a uniform bankruptcy scheme that would guard against legislating so narrowly that it would enable this type of discrimination, and thereby, would be able to protect national commerce. And that purpose is fully advanced by having the uniformity requirement apply in the territories.

Puerto Rico, of course, has long participated in the national market for municipal debt. It's issued many, many

billions of dollars in bonds that are held by creditors throughout the nation. And, of course, these proceedings will affect the interest of investors and creditors around the nation.

So inventing bankruptcy laws for the territories from the uniformity requirement we think would harm national commerce by undermining the predictability and fairness of commercial regulations. It would harm the very debt market that Puerto Rico wants to gain access to again. And there's no practical impediment to applying the bankruptcy uniformity laws in the territories.

This isn't like the example of the territorial courts, unlike tenure. In fact, Puerto Rico was subject to a Chapter Nine bankruptcy for many decades, and there were no suggestions that that created any kind of practical problem or otherwise infringed on the flexibility that Congress might otherwise need with respect to the territories.

The emphasis on the purpose of Article IV, to give Congress flexibility as a general matter, it doesn't answer the question of why Congress specifically needs that flexibility to depart from the uniform Bankruptcy Rules in the territories. And so the Supreme Court analysis in *Aurelius*, we think has equal application here.

With respect to the Appointments Clause, the Court said, why should it be different just because the law relates

to Puerto Rico and other Article IV entities. We don't think that there's any good answer to that question here.

I want to make a final point in response to the arguments relying on tax uniformity precedent. And Mr. Humphreys has also referred to the naturalization precedent. At the outset, as I've mentioned, this is a provision-specific approach. The Supreme Court has never applied a one-size-fits-all analysis to the various constitutional provisions. And instead, in all of these cases, it's looked at the purpose of a particular provision and analyzed whether that should apply in the territories.

So at the outset, naturalization uniformity serves a different purpose. There would be practical obstacles to applying those naturalization rules across the board to territories, when some may actually disassociate from the United States and no longer have a political relationship, others might become ever closer and maybe achieve statehood.

Tax uniformity also serves a different purpose. It's about making sure that Congress doesn't favor certain states over others. So it's not intended to standardize creditor relief in the same way that bankruptcy uniformity is. And Congress' taxing power as well wasn't intended to preempt state tax authorities.

States, of course, have wide variation in their tax schemes today, and that's why cases like *Binns* could recognize

that Congress can create local taxes that reflect that same divergence, because any state or locality could do the same thing. But more fundamentally, the tax uniformity precedent traces back to the Supreme Court's decision in *Downes versus Bidwell*. And this, of course, was one of the Insular Cases.

Those cases have been wholly discredited. They rest on the racist colonial theories that inhabitants of territories are members of an alien race, that effectively inhabitants of territories aren't entitled to the same kind of constitutional protection as other citizens of the United States. And so the analysis in the tax uniformity precedent, and specifically Mr. Humphreys had emphasized this throughout the United States' language, that goes directly back to the view that you could treat territories as not being part of the United States, because of this alien race theory that is wholly discredited.

In the First Circuit, of course, and the Supreme Court have both said that the Insular Cases should not be extended. So our submission is that it wouldn't be proper to reflexively apply on tax uniformity precedent here -- those precedents serve a different purpose, and to try to extend their analysis automatically to bankruptcy uniformity we think would represent an extension of the Insular Cases that the Supreme Court has already disavowed.

This really actually comes full circle to the

Oversight Board's assertion that statutes passed pursuant to Article IV are, therefore, local laws, which therefore means that Congress can do whatever it wants with the territories, even if there would otherwise be constitutional restrictions on its authority. That would be perhaps the biggest extension of the Insular Cases of all, and it's not the law. The Supreme Court has rejected it. The First Circuit has rejected it. And we would ask this Court to reject it as well.

I'd like to turn now to the substantive uniformity argument, and move on to our arguments that Puerto Rico -- I'm sorry, that PROMESA violates the uniformity requirement. Mr. Humphreys at the outset has emphasized that Congress has flexibility under the uniformity requirement, but uniformity is not toothless.

I'm sorry, Your Honor. Can you hear me?

THE COURT: Yes, I can. I'm sorry. I'm just trying -- I interrupted you a couple of times, and I'm trying to restrain myself so that you can speak.

MS. PRELOGAR: I'm sorry. For some reason I wasn't lighting up on the screen dashboard, so I was worried that I had lost the connection.

THE COURT: No. I hear you very clearly.

MS. PRELOGAR: Excellent.

So as I was saying, the uniformity requirement isn't toothless. If you look at Supreme Court precedent, you can

distill two different types of restraints, and PROMESA here violates each of them. First, the Supreme Court recognized in the *Gibbons* case that Congress cannot legislate for such a narrow class of debtors that it effectively constitutes a private bankruptcy bill.

In *Gibbons*, Congress had passed a statute for a particular railroad bankruptcy, and had given priority to the claims of one group of creditors, the employees, over other groups of creditors, the bondholders. And what the Supreme Court said is that the statute was problematic, because Congress had legislated too narrowly; that it was effectively attempting to address the problems of one regional railroad, rather than to create a set of rules that could apply equally to all creditors and all debtors in a class.

And then the second requirement that the Supreme Court has recognized is one of geographic uniformity. Of course we acknowledge, and it's come up here again several times today, that Congress can respond to geographically isolated problems, for example, with respect to industries. So if you can imagine, if an industry was clustered in one region, Congress wouldn't, on that basis alone, be disempowered from acting. But Congress can't define the problem as one of geography itself, or else it would end run the basic bankruptcy policy of guarding against geographic discrimination.

And just to try to make this more clear with a concrete example, if Congress created one bankruptcy scheme for California, and then a different bankruptcy regime for New York, that would aim at the very evil that the Bankruptcy Clause is intended to address. And so those kinds of explicit geographic distinctions in bankruptcy laws are disapproved.

Now, the Oversight Board relies on *Blanchette,* and notes that there there was a geographic definition in that statute; that in *Blanchette*, the railroads that were covered by that statute were defined in terms of the region where they operated. But the critical thing to recognize is that the geographic definition in *Blanchette* was effectively shorthand, because it was possible to define that debtor class without reference to geography. The Supreme Court emphasized that fact. The Court said, this law applies to all relevant railroads then operating across the United States, and for that reason, the Court could conclude that it operated uniformly with respect to the debtor class, and also uniformly with respect to all creditors of the debtor class. In other words, that the definition of the region there didn't obscure that this was actually a law that was uniform throughout the United States.

But here PROMESA transgresses both of these limitations. It's effectively a private bankruptcy bill for Puerto Rico, and Puerto Rico is a geographically defined

debtor. There can be no real dispute that Puerto Rico stands alone in having access to the unique Title III discharge of debt proceedings in PROMESA.

There was a brief argument, I believe, in the briefings by the Retiree Committee and the United States that the statute defines the word "territory" to include other territories. But the critical point is Congress purposefully excluded those other territories from PROMESA, and made clear that, in that way, only Puerto Rico would have access to PROMESA's debt adjustment process.

And then as well, geography alone determines the statute's coverage. There's no way to describe the debtor class subject to PROMESA without using that geographic definition. And Congress recognized this problem that there is emphasis. In Section 3(b), this is a severability provision, Congress expressly noted that PROMESA could be invalidated as a nonuniform bankruptcy statute in recognition that PROMESA applies to Puerto Rico and not to a broader debtor class.

So although we recognize that Congress has flexibility under the bankruptcy uniformity requirement, looking at the specific limitations that have been acknowledged in the case law, we think that PROMESA violates both of them.

Now, the Oversight Board has emphasized, and it came

up again this morning, that PROMESA applies not just to the Commonwealth, but also to the instrumentalities. And the problem with that argument is that the debtor class here is defined in express terms about the entities' relationship to each other, and again, it's defined in express geographic terms. So it's not like this is a statute that is aimed at a particular industry, or a statute that aims at particular status, like municipal status.

I think Mr. Bienenstock ticked off a long list of different types of industries that had been regulated under bankruptcy law, but here the debtor class is expressly defined in terms of the relation of the class of debtors to one another. The Section 511 defines Puerto Rico as the Commonwealth and its instrumentalities. Section 519 defines the instrumentalities as being part of the territory. And PROMESA further underscores its relationship in a variety of ways.

We've emphasized, of course, that the Oversight Board serves as the sole statutory representative of all the governmental entities in Puerto Rico. And this Court, the First Circuit, have both said and emphasized that the Board can carry out those duties in a holistic manner. So in taking steps on behalf of the instrumentality, it can consider the interests of the Commonwealth as well. And as a practical matter, this is, I think, also critically important. The

financial interests of the Commonwealth and the instrumentalities that are being adjudicated in these Title III proceedings have been found by the Court to be intertwined in various respects.

The Oversight Board made this clear in the COFINA proceeding when it said multiple times that COFINA had to go forward first as a gating item in the *Commonwealth* case, because whether the sales and use taxes were the property of COFINA or available resources of the Commonwealth was one of the critical, dominant, disputed legal issues in the case. And as a practical matter as well, the Commonwealth has exercised substantial control over revenues that are owed by statute to the instrumentalities.

Your Honor is well aware Ambac's objected to that and believes it's unlawful; but for present purposes, it shows the relatedness of the debtors covered by PROMESA, and underscores that this law implicates the same concerns as a private bankruptcy bill. Because if Congress is permitted to legislate so narrowly, if it can effectively define a debtor class in terms of this express relationship between the debtors, as here, then it can discriminate against creditors and undermine national commerce in ways that the founders aimed to prevent through adoption of the uniformity requirement.

It would be, for example, no different than

legislating private bankruptcy relief for members of one family, or to legislate a private bankruptcy bill for all the governmental units of just one state or one city. When the relationship between the debtors is the defining element of the class, then the interests in *Gibbons* equally applies. And the interest in avoiding the possibility of discrimination, and in protecting national commerce, we think should carry weight.

The Oversight Board has also argued that PROMESA was simply a response to a geographically isolated problem. And we think that that is flawed both factually and legally, so I'd like to briefly walk through each of those points.

Factually, Puerto Rico was not the only territory in financial distress when PROMESA was enacted. As we've explained in our briefing, Guam and the U.S. Virgin Islands had, likewise, seen their debt-to-GDP ratios balloon. Both of those territories had outstanding pension obligations that could raise questions about whether they would be able to continue their debt service at existing levels.

In early 2017, the U.S. Virgin Islands actually had more debt per capita than Puerto Rico. I believe it had 19,000 dollars per person, whereas Puerto Rico had 12,000 per person. And, in fact, the Virgin Islands had lost access to capital markets at favorable interest rates, and some of its bonds had been downgraded to junk status.

So the suggestion here that Puerto Rico stood alone, that it was the only territory that was in financial distress, or that could conceivably at some point need access to restructuring relief, is belied by the facts and the existence of other crises in other territories at the same time. But the more important point I think is the legal one, which is that if Congress could really draw these kinds of fine distinctions, and could say that Puerto Rico can have this bankruptcy bill, because it's most in need of reorganization, and it, therefore, can constitute its own debtor class, that would effectively mean that there's nothing left of the bankruptcy uniformity requirement.

At that point, Congress could always define the problem narrowly, and it could create nonuniform laws down the line by identifying each particular debtor, looking at that debtor's financial situation, trying to identify characteristics that it thinks warrant a bankruptcy bill, and then creating that bankruptcy bill. And if that's all that that uniformity requires, is for Congress to identify the particular problems of a particular debtor, and then try to address that particular issue, the uniformity would have very little application at all.

It's also not clear that this should even be about present financial distress. So this is the test the Oversight Board has offered where they focused on the notion that Puerto

Rico was most in need of restructuring, but the problem with that is that these kinds of bankruptcy regimes should be forward looking. The whole point is to create a uniform and stable set of rules about how the market is going to operate. And that's, of course, how Chapter Nine bankruptcy works.

In the Chapter Nine context, there is a set of rules, and municipalities and their creditors know those rules. Notwithstanding the fact that some municipalities may never need bankruptcy relief at all, the statute is not focused on kind of -- that present financial situation.

So for those reasons, we don't think that PROMESA can be justified here as a response to a geographically isolated problem without essentially reducing the scope of the uniformity requirement in ways that contrast sharply with what the Supreme Court has recognized is available under the uniformity requirement.

Finally, I want to briefly respond to Mr. Bienenstock's point about the asserted similarity between PROMESA and Chapter Nine. And at the outset, I want to emphasize that of course PROMESA creates a fundamentally different set of rules for Puerto Rico as compared to all other territories, because no other territory has access to court-supervised debt restructuring at all. The other territories are boxed out of and closed out of having bankruptcy relief.

And so in that sense, just thinking about the comparison, PROMESA creates an entirely different set of rules for Puerto Rico as would be applied in any other territory, and that is one of the relevant distinctions that we think matter for uniformity purposes. But even just looking at Chapter Nine, there are a number of differences between the scheme that PROMESA creates and other bankruptcy laws, and they fall into -- we've listed a number of provisions in our Complaint and discuss a number of provisions in our briefing.

I wanted to quickly walk through the three principal categories of difference that we see. The first is PROMESA's plan confirmation provision. This is Section 314(b)(7). Mr. Bienenstock discussed it as well. This is the provision that provides that a plan can only be confirmed if it's consistent with the Board's certified fiscal plan. And the fiscal plan provision, which is Section 201, then settles, establishes exclusive requirements for allocating funding among the Commonwealth's creditors.

And the Board has said that it can interpret and apply those requirements in its discretion, but the issue here and the problem we perceive is that the fiscal plan then becomes a critical input into the plan of adjustment. And that has no comparable analog in Chapter Nine. There's no equivalent to 314(b)(7) in Chapter Nine at all.

The fiscal plan isn't just projection. It's

determination by the Oversight Board about how much money the Commonwealth can expend to service its debt, and how to allocate that funding among different creditors. So this really does, in our view, raise the risk that the fiscal plan will essentially be used to set a benchmark for feasibility in a way that differs from other municipal bankruptcies. And that's the first category.

The second category is the limitations on judicial review. So this comes from Section 106(e). It applies, of course, to the Board's certification decision and its certification of the fiscal plan. But the Board has suggested it has authority under PROMESA to allocate the Commonwealth's revenue among creditors in a manner that it asserts can't be reviewed at plan confirmation. And if that were true, that would be another substantial difference between how Chapter Nine operates and how PROMESA works.

And then the final category I would point to is the role of the Oversight Board itself. The Oversight Board, again, is the sole statutory representative for all of the debtors. It has taken over the functions in this bankruptcy proceeding that would otherwise, in the Chapter Nine context, be exercised by state and local officials. And those state and local officials would not have the same conflict of interest that we perceive the Board to have. They also would be politically accountable in a way that the Board is not.

They would be accountable to the public, to creditors, and to their constituents. So, in that sense, we think that there are any number of differences between PROMESA and Chapter Nine that are relevant here.

In its briefing, the Board suggests that, actually, the Court shouldn't look at Titles I and II of PROMESA at all. Instead, the Court should just focus on Title III. Of course, just focusing on Title III, there are fundamental distinctions, as I just mentioned, for example, with the plan confirmation provision. More fundamentally, these are an integrated bankruptcy scheme. Title III itself incorporates and relies on Title I and Title II authority.

So as I just mentioned, of course, the plan confirmation provision directly incorporates the Board's certified fiscal plan by requiring that consistency with the fiscal plan for purposes of confirming the plan. And Title I, in the existence of an Oversight Board that's created under that provision, itself provides the gateway to the bankruptcy proceedings, because absent having an Oversight Board created in accordance with Section 101 of PROMESA, an entity isn't entitled to adjust its debt under the statute at all.

So in that sense, we think that these provisions all do form an integrated scheme. And I would point as well to Congress' own determination in this regard. Congress expressly linked these provisions for purposes of

severability. It provided that if Title III is invalid, then Titles I and II of PROMESA should be invalidated as well. So we think that's further evidence that Congress itself viewed these provisions as operating and working together, in tandem, to create the debt adjustment scheme that's at the core of PROMESA. But it also means the severability provision -- that this issue is a little bit academic, because whether or not the Court looks at Titles I and II, for purposes of assessing the uniformity, it's clear that Title III is a bankruptcy statute; that it addresses the subject of the relations between debtors and creditors; and for that reason as well, the severability provision and the lack of the possibility of severability demonstrates that all three of these titles have to rise or fall together.

My final point on this is just to emphasize again that Congress itself recognized that a court could find PROMESA to be nonuniform. That's why it included the language in Section 3(b), specifically acknowledging that a court could hold that PROMESA is invalid as a nonuniform bankruptcy statute. We think the Court should reach that conclusion here.

Now I'll turn, unless the Court has questions, to the severability issues. And I'll be brief on this, because the parties' briefs discussed this in full. There hasn't been a lot of discussion about it at the hearing this morning, but I

did want to quickly touch on our perspective on why the Severability Clause cannot be implemented in this case.

So Section 3(b) is a provision where Congress recognized at the outset that PROMESA could be declared unconstitutional, but then said that the fix here is that the Court shall extend PROMESA -- and this is a quote -- to any other similarly situated territory, end quote, that requests the establishment of an Oversight Board. We don't think that fix can be implemented. And there are really two key problems to focus on.

The first is that Congress didn't define what characteristics or criteria should be used to determine if a territory is substantially similar, and that's a legislative judgment. It goes to the question of what the debtor class should be, which entities PROMESA should cover in the first place. That's the legislative domain to determine exactly what the scope of the debtor class should be for bankruptcy purposes.

And it's not as though there's only one way to draw the line. One possible way would be to say that all territories should be covered, that, basically, the status of being a territory is itself the similar situation that the territories confront. But there are other ways. The Oversight Board has suggested that the level of financial distress should be relevant. And then that raises the

question, well, what is the relevant level? Is it with a metric? Is it debt-to-GDP ratio? Is it having bonds downgraded to junk status? Is it losing access to capital markets? Our submission is that those are questions for Congress to answer.

The Oversight Board suggests that the Court would have to consider substantial similarity as part of adjudicating the claim in the first place, but that's not actually how uniformity analysis proceeds. It's not necessary to consider what lines Congress could draw, or to go beyond and try to dictate for Congress how it has to legislate on a more uniform basis. That's not the role of the Court. Instead, what the Court does in a uniformity challenge is to look at the lines that Congress actually did draw and adjudicate their constitutionality.

And then finally, even if it were possible to get past this hurdle and to identify the similarly situated territories, the problem is that there is no way to implement the Severability Clause without adding words and provisions to PROMESA that aren't currently there. So, again, under Section 302, an entity can only qualify as a debtor if it has an oversight board established for it under Section 101. And this is a limitation that's repeated throughout other provisions of PROMESA.

So, for example, in Section 5(7), this is another

definitional provision, a covered territory is defined as a territory for which an oversight board has been established under Section 101. But the problem is that if you've looked to Section 101, there's no provision there that provides any mechanism to establish an oversight board for any other territory. Section 101 is focused and creates the Oversight Board for Puerto Rico alone.

So that means that to try to implement this severability fix, the Court would have to actually add words to the statute, add provisions to the statute that aren't currently there, and add this mechanism into Section 101. And that's not how severability analysis generally works. It's about striking words from a statute and removing an unconstitutional provision. It's not about adding provisions that aren't currently there.

The other side has invoked cases like *Barr versus American Association of Political Consultants*, but that actually reflects the traditional way that severability works. There, there was an unconstitutional limitation in a statute that the Court can strike, and it had the effect of expanding the statute's scope. But the Court didn't add any words to the statute to do that.

This stands in sharp contrast, and I'll just note that we really boiled the ocean here in looking for comparable situations where either a Severability Clause like this

exists, or where courts have considered and -- considered whether to enforce such a clause, and we couldn't find anything. This is a really unique kind of provision. And ultimately, although Congress recognized the uniformity problem inherent in PROMESA, it didn't provide an appropriate mechanism for the Court to fix it itself. That has to be the work of Congress, to draft the uniform statutes that can provide bankruptcy relief to Puerto Rico and a wider debtor class.

THE COURT: I do have a question for you about this. If the Court were to take Congress at its word, and extended the statute, using the words of Congress, to similarly situated territories that request an oversight board, by the structure of PROMESA, the territory, the would-be similarly situated territory can't get any further until it has an oversight board, because, otherwise, Title II doesn't operate and the Title III petition can't be filed.

So doesn't that language essentially funnel the threshold question of what territory is sufficiently situated -- similarly situated to merit an oversight board, back to Congress, so that Congress is making the determination as to whether the particular territory is eligible, but what the Court would be doing would be taking up Congress' invitation or grant of permission to open this line of application back to Congress under this statute?

So it seems to me that Congress is not requiring the Court to decide who is similarly situated today, except that it would have to be a territory, and giving Congress the opportunity to make the finer distinctions on a particular record with respect to a particular territory. So why is that a problem?

MS. PRELOGAR: Well, I think it's absolutely right that Congress would be best positioned and is the only entity with authority to make the determination about which territories are similarly situated. So what that means is it would require further Congressional action to expand PROMESA's scope and to ensure that there were other territories that had access to bankruptcy.

And, in fact, in the drafting history, originally, Congress had drafted this to provide a mechanism in Section 101 for other territories to have oversight boards established for them, but Congress expressly removed that provision from the statute before finalizing PROMESA. And that's what ultimately turned this into a statute that was focused only on Puerto Rico.

If I'm understanding Your Honor's question correctly, I think the problem is that this really does have to go back to Congress. So there's no way for the Court itself to determine the similarly situated territories and then add that provision to PROMESA. That's what all the parties have

understood the Severability Clause to dictate. And it's not an enforceable remedy. This means that it would have to go back to Congress, and then Congress could take that action and make the determination about how to legislate with a broader debtor class in mind.

THE COURT: Thank you.

MS. PRELOGAR: I'd like to turn now to the procedural issues in the case, and I want to begin with laches in particular. And I want to respond to the allegations that the suit is untimely.

There have been a lot of words thrown around in the briefing that this was strategic delay, that this was gamesmanship on Ambac's part, and I want to push back forcefully on that characterization. The critical thing to recognize here is that -- the way that the injury to creditors, and to Ambac in particular, has become more apparent and more concrete over time through the course of the proceedings.

So it's not as though Ambac was immediately injured in a concrete sense, in a practical way, by the fact that Congress passed this nonuniform statute. We're not purporting to be constitutional purists who just have an abstract or academic interest in ensuring that Congress stays within constitutional limits. Instead, we're arguing that Congress exceeded those limits in a manner that over time has enabled

the Oversight Board to discriminate against creditors in profound ways that finally prompted Ambac to file this suit.

And litigation like this is an investment. There's always a question of whether it's worth it to bring a case. In the beginning, and in the prior phases of this proceeding, it wasn't fully apparent how these nonuniform provisions of PROMESA would be interpreted, or what authority the Board would seek to claim under the provision. This was a novel thing for us to see. There wasn't anything exactly like it.

And earlier on, in fact, the Board adhered far more closely to normal bankruptcy procedure. For example, in the COFINA Title III, the Board appointed an independent representative to represent COFINA, that thus eliminated the same concerns about conflicts of interest. And it also wasn't clear in the beginning exactly how PROMESA would be interpreted, what some of these nonuniform provisions would mean in practice, what practical effects they would have. But as time has gone on, as we've received additional decisions from this Court and from the First Circuit, it's illuminated the meaning of those provisions.

And I'm thinking here, for example, of decisions about Section 106(e), and the nonreviewability of the Oversight Board's fiscal plan. Of course, there have been the decisions I referred to earlier from this Court and from the First Circuit on the holistic approach that the Board may

employ in these proceedings.

As this Court knows, Ambac's resisted many of these interpretations at nearly every turn. But the point is that PROMESA's nonuniform provisions, as they have been interpreted, have made far more clearly the various ways in which PROMESA operates differently from other bankruptcy laws.

And the other relevant change here has been how the Oversight Board has, over the course of the Title III proceedings, itself taken increasingly expansive positions about the authority that it thinks has been granted under PROMESA. Those positions have themselves brought into sharper and more concrete focus the harms that are caused by the lack of uniformity.

So, for example, the Board's theory of preemption has evolved over time, and now the Board is arguing that PROMESA preempts all pre-PROMESA territorial law. But the Board's further saying that it can selectively invoke that preemption rationale to, in essence, choose for itself, pick the winners and losers of which creditors to favor in the Title III proceeding. And that's culminated in the Proposed Plan of Adjustment that we're currently reviewing, that gives 90 percent recovery to the pension claimants, and then gives nearly all of the remaining plan consideration to the GO bondholders, while revenue bondholders would receive less than one percent on their claims.

So, you know, ultimately, when a party's injury like this becomes more pronounced or more apparent over time, courts have recognized that laches shouldn't stand as a bar to the suit. And I would point the Court in particular to the decision in *Garza*. This is a decision we cite from the Ninth Circuit that involved an unconstitutional redistricting plan.

There the Ninth Circuit recognized that the plaintiff's challenge to the plan was on its face, and could have been brought at the moment the plan was adopted; but the plaintiffs had waited to see how the injury would develop, what that plan would produce. And it wasn't until after several election cycles, when it became clear that that plan was producing serious concrete injury, that the plaintiff filed suit. And the Ninth Circuit has said that that period of delay was justified given the way that the facts on the ground had shifted.

A contrary rule, of course, would force litigants to file suit instead at the earlier possible moment, so incentivize, essentially, constitutional litigation, and discourage waiting and any possible voluntary dispute resolution.

The other point I want to make on the laches claim is that the arguments to laches really ignore the legal framework here that applies to claims like this one where we're seeking prospective relief for an ongoing injury, and it's really

important to emphasize that context. Our argument here is that PROMESA is an unconstitutional statute that creates ongoing injury, that didn't just happen at one discrete moment in time when Congress passed the statute, but rather creates the potential for harm that exists and continues to this day.

And courts are cautious about applying laches to claims for prospective relief generally, but especially to an unconstitutional statute that affects a wide variety of people. But part of that is the practical recognition that the harm truly can't be said to be remote in time in that instant. You know, the typical case of laches, the harm happened at one point in the past, many years have elapsed, and then the plaintiff seeks a retrospective remedy. And there there might be prejudice, because witnesses memories might fade, documents might have gotten lost, and so that's kind of the quintessential application where laches has been held to apply.

But there's a fundamental difference when there's an ongoing constitutional injury. And, again, *Garza*, the Ninth Circuit case I've referred to, recognized this principle and held that even though the plaintiff had waited years to challenge the unconstitutional redistricting plan, laches didn't bar the claim.

There's a practical component as well, of course, because if an unconstitutional statute remains in effect, then

it could trigger a new lawsuit at any time. There's not the same idea or prospect that there's a discrete past injury that happened so long ago that now the parties' rights have kind of become settled through the passage of time.

Here, for example, imagine if the Oversight Board were to file a new Title III tomorrow, let's say for PRIFA. There would be no argument that a uniformity challenge could be barred in the context of that Title III. So there's no way to get the repose of the laches doctrine in that. There's no way that -- have it be a concrete past dispute that's settled. The only way to get the repose is to actually adjudicate the constitutional issue and decide whether or not PROMESA is a constitutional bankruptcy statute.

Just one final point on laches with respect to prejudice. Mr. Friedman had mentioned that the money that the parties have expended is part of the Title III proceedings, but it's important to recognize that laches looks at whether the delay itself is what caused the injury. It's almost like a detrimental reliance kind of inquiry. And here there's just no reasonable argument that these fees would not have been expended if the suit had been filed earlier.

The Appointments Clause litigation was pending the whole time. Other challenges, of course, had been pending. And it hasn't stopped the Oversight Board from pressing forward, so I don't think there's any real argument to be made

that the Oversight Board would have discontinued its efforts in these Title III proceedings if only the suit had been filed earlier. And for that reason, we don't think laches can bar this suit.

I'll turn now to the estoppel doctrine. I want to emphasize at the outset, Mr. Friedman has kind of generally referred to equitable principles, but these are doctrines, narrow doctrines with distinct elements. And here, down the line, none of the elements of constitutional or judicial estoppel are satisfied.

So just focusing in on constitutional estoppel for a moment, the Supreme Court has made clear that the statute has to create a unique benefit that didn't previously exist, and then the litigant has to voluntarily elect to receive that benefit, so essentially opt into the statute for a scheme in the first place. You can't choose to receive a benefit and then seek to remove conditions on the receipt of the benefit under the statute. It's basically the articulation the Court has adopted.

But here there's no benefit in the first place. PROMESA doesn't create new or special rights for creditors. It, in fact, provides a debt adjustment mechanism that interferes with their pre-existing rights. So it stands in sharp contrast to cases where the Court has concluded that there was a statutory benefit.

For example, *Robertson versus FEC*, the Oversight Board cites this case, that was a statute that created a pool of money for presidential candidates who could voluntarily choose to accept those matching funds. There's nothing like that here. Their sole argument is that Ambac obtained a benefit in COFINA based on the amounts it lists in terms of the COFINA Plan.

But the Board ignores that Ambac was owed more than it was paid. And there's just no case suggesting that a bankruptcy statute that authorizes the discharge of debt and impairs the obligation of contracts can instead be characterized as a benefit to creditors for estoppel purposes. It essentially requires changing the frame of reference and saying, well, Ambac could have been paid even less.

And that's essentially what the argument is here, that in a world without PROMESA, Ambac is actually better off now in the grand scheme of things, but that's just not how constitutional estoppel works. And I point the Court to the Supreme Court's decision in the *Kadrmas* case. This was the school bus fee case.

There the argument was made that absent that school bus statute, the plaintiff would have had to pay even more money, because private bus transportation costs ten times the amount of the public bus fee. And the Court rejected that argument and said, you can't characterize a benefit in that

way. We think the same argument applies here.

There's also not the same showing of voluntariness. Ambac, of course, had no control over whether to become subject to PROMESA. It was the Board that decided in its sole discretion to file the Title III proceeding in PROMESA -- I'm sorry, for COFINA. And at that point, of course, Ambac tried to defend its rights and interests in the context of the COFINA proceeding, but we've cited ample precedent that emphasizes that when a plaintiff seeks to protect its business interests under a statute that it had no choice to become subject to in the first place, it is not estopped. And those cases include *Abie*, *State Banks*, also the *Union Pacific Railroad Company* case.

Turning quickly to judicial estoppel, the key problem here is there's no directly inconsistent position. Ambac has never argued that PROMESA is not subject to bankruptcy uniformity. It's never argued that PROMESA satisfies bankruptcy uniformity. That issue just hasn't previously been presented, discussed by Ambac, or adjudicated by this Court.

The theory of judicial estoppel rests on a single filing in the COFINA proceeding, where Ambac was addressing a different issue, a discrete issue this Court had posed about whether the Court had authority to rule on the validity of the new bond legislation. But that was a question of statutory authority or inherent authority of this Court to be able to

consider Commonwealth law. There was no issue presented of whether Congress had validly passed PROMESA under the bankruptcy uniformity requirement. And that's an important thing to recognize.

The First Circuit precedent required a directly inconsistent position, a mutually exclusive position. So, for example, in the *Lydon versus Boston Sand and Gravel* case, which we've cited, the litigant said in the first proceeding the state law provided the exclusive remedy --

(Sound played.)

MS. PRELOGAR: -- and then turned around in the second case and argued that federal law provided the exclusive remedy. That's a case where a litigant took a directly inconsistent position on the exact issue that was presented, and the Court held that judicial estoppel could apply. But this case is far more comparable to the ones we've cited, where the allegation instead is that there's been some kind of implicit change of position, and that the Court should read something into that.

I would point the Court to the *RFF Family Partnership* case, which we think demonstrates, based on very similar reasoning, that there's just no argument here that the directly inconsistent position prong could be satisfied.

I'll make just one quick point about the contractual bar claim. The Oversight Board didn't mention it today, and

practically abandoned the claim in its Reply Brief. And we think that's for good reason.

There's no showing here that this lawsuit in any way violates the COFINA Plan Support Agreement. The COFINA Plan became effective nearly two years ago now. The Plan Support Agreement has terminated, and by its own terms, it has no continuing effect. That comes from Section 6.1(b) of the Plan Support Agreement, which says that the agreement was over when the Plan was substantially consummated. That was back in February, 2019. And it also comes from the Section 6.2 provisions that expressly state that, after termination, all the other provisions are null and void and have no force and effect. It lists some provisions that survive termination, but the contractual claims that the Board is pressing here isn't included on that list.

The Oversight Board doesn't engage with the contractual terms at all. We think the terms are clear, and squarely foreclose the Board's claims. But I should just emphasize, as my final point, that even if the PSA were still in effect, this suit does not violate it, because the COFINA Plan has been consummated and can't be undone. The old bonds have been canceled. The new bonds have issued. They've traded on public markets. The distributions have been made.

(Sound played.)

MS. PRELOGAR: So for that -- so I will just conclude

by saying that --

THE COURT: Yes, please finish your sentence.

MS. PRELOGAR: Thank you. Thank you. I appreciate that.

That there's no real claim here, nor could there be, that there's a contractual violation. And for these reasons, there's no basis to dismiss the Complaint, and we would respectfully request that you deny the Board's Motion to Dismiss.

THE COURT: Thank you, Ms. Prelogar.

MS. PRELOGAR: Thank you.

THE COURT: We will now turn to the rebuttal arguments, and first up is the Retiree Committee for five minutes.

MR. GERSHENGORN: Thank you, Your Honor. Ian Gershengorn again.

I just want to make a few quick points. First, with respect to whether the Uniformity Clause applied, Ambac contends, and you've heard this morning that our position is based on the idea that all constitutional constraints are inapplicable; there's an on-off switch or a categorical bar. But as Your Honor observed, that is not our argument. Our argument is specific to the Bankruptcy Clause and the bankruptcy uniformity provisions.

So to be clear, we think that it doesn't apply for

two main reasons: One, because the Bankruptcy Clause is not a structural limit on all federal power, but instead a tailored limit on a particular enumerated Article I power. And, second, because the Supreme Court and other courts have already held that the other uniform provisions in the Revenue Clause and the Naturalization Clause do not limit Congress' powers in the territories.

Second, Ambac said we don't identify any reason not to apply the Bankruptcy Uniformity Clause to the territories, but that simply isn't true. There's a very clear reason, and that is, the point of Article IV is disuniformity. It is to give Congress a wide berth for inventive statesmanship.

As the Supreme Court has said, it's intended to give broad latitude to develop innovative approaches to territorial governance. Presumably, that is exactly why the Court has not applied the uniformity provisions of the tax -- of the Revenue Clause, and why courts have not apply the uniformity provision of the Naturalization Clause to the territories.

In response, and this is my third point, Ambac says that somehow you should distinguish between the Revenue Uniformity Clause and the Naturalization Uniformity Clause on the one hand, and bankruptcy on the other. But that is flatly wrong. First, the text is exactly the same for all three provisions. It would be an extraordinary means of constitutional interpretation to interpret the exact same

clause in neighboring provisions in diametrically opposed ways.

Second, of course the Court itself has looked to all three clauses when interpreting each other. That was true in *Blanchette*, and it was true in *Ptasynski*, in which in both of those cases, the court looked to the other provisions in interpreting the provision before it. All three provisions use the same text, and the Court ostensibly interpreted them all of a piece.

Third, Ambac says that you shouldn't rely on *Binns* and the Revenue Clause, because it's an extension of the Insular Cases, but that is simply not the case. In fact, *Binns* itself, which applied, of course, to Alaska, started the analysis by saying on page 490 of the opinion, it is unnecessary to consider the decisions in the Insular Cases, though it is clear that *Binns* is not an Insular Case and that the logic in *Binns* controls this Court.

And fourth, on this point, Ambac says that *Gibbons* makes clear that the Territory Clause can't be used to, quote, unquote, override the Bankruptcy Clause. But in *Gibbons*, it was a very different issue, because reliance on the Commerce Clause there would have rendered the uniformity --

(Sound played.)

MR. GERSHENGORN: -- entirely null and void. But, of course, that's not the case here.

If you apply -- if you don't apply uniformity to the Territories Clause -- the Uniformity Clause of the bankruptcy provision has ample scope, the scope it has always had, to prevent discrimination among the United States.

Let me turn now to whether this is a local statute. Again, Ambac mischaracterizes our argument by saying, we think any time Congress invokes Article IV, that's a local statute. That is not our position. Our position is that this is, by its terms, a local law. We think *Aurelius* makes that clear.

Ambac says that *Aurelius* held something different, and of course they do, but *Aurelius'* discussion of whether officials' duties were primarily local is obviously relevant to whether PROMESA itself is local. And what the Court said was the Board's duties are "quintessentially local," because they, quote, concern the finances of the Commonwealth, not the United States.

Ambac then repeats its argument that a state legislature could not pass it, but that misunderstands Congress' territories power. What the Court has said is Congress has, quote, full and complete legislative power over the people of the territories, and practically unlimited powers of legislation over the territories.

Finally, let me address Ambac's argument that this is somehow a private bill. I believe counsel said this is like an act for a single family. Well, of course Puerto Rico

provides services to three million people, and Congress found expressly that fiscal emergencies were limiting its power to do so. That is nothing like a family or a single railroad.

I also want to say, in *Ptasynski*, one of the things the Court said that really hasn't gotten a lot of play here today is that whereas here Congress has exercised its considered judgment with respect to an enormously complex problem, we are reluctant to disturb its determination. It seems to me that the Supreme Court's wisdom there with respect to the Uniformity Clause and the revenue -- the uniformity provision in the Revenue Clause applies directly to the issue before this Court today. The uniformity provision was not intended by Congress --

(Sound played.)

MR. GERSHENGORN: -- to -- nationwide enactment to deal with local conditions. We think that Ambac's arguments here today are non-persuasive, Your Honor.

Thank you, Your Honor.

THE COURT: Thank you, Mr. Gershengorn.

We now have rebuttal from AAFAF for two minutes.

Mr. Friedman, I think you need to unmute. Remember it's both the dashboard and your phone.

Mr. Friedman, I'm still not hearing you.

MR. FRIEDMAN: In order to --

THE COURT: There you are.

MR. FRIEDMAN: Thank you, Your Honor.

I have a lot to say. I'm going to try to say it as clearly as I can.

The first is that Ambac has completely ignored that it brought a facial challenge to that institute. There was no response to that argument. If you go back and read its original Complaint, starting from day one of this case, they have complained about Section 106; they have complained about illegal fiscal plans; they have complained about unlawful takings. None of that has changed. And the argument that somehow things are different now is just incorrect.

Second of all, Ms. Prelogar completely misunderstands the conflicts and holistic approach decisions of this Court and the First Circuit which relate to established principles under Chapter Nine, that this Court and the First Circuit have cited and do not rely entirely on PROMESA precedents. So it's just inaccurate to say that those have only evolved over time. Those relate to Eighth and Ninth Circuit decisions that interpret, excuse me, Chapter Nine for years.

The third point I want to make is that certainly Ambac could have acted more quickly on this. It could have sought injunctive relief. So the idea that it didn't delay is untrue.

The next point I want to make with respect to laches is Ms. Prelogar cites the *Garza* case, but of course that case

had nothing to do with ongoing restrictions. The plaintiffs there wanted to go in and seek, for example, to revoke the votes of legislatures that had been effected under prior districts. That would be the equivalent of the remedy sought here. This is to destroy an ongoing project.

There was no response to arguments about rejecting contracts or rights that have already been determined. Only a focus on fees. And speaking of fees, Ms. Prelogar completely ignored the fact that her client signed up to the Plan Support Agreement with COFINA, not to receive benefits under a plan of adjustment, but to receive unique and special benefits in securities design and payments of tens of millions of dollars of legal and professional fees. That's not being a simple recipient of a plan treatment.

(Sound played.)

MR. FRIEDMAN: That is being a strong proponent of a plan.

Your Honor, if I may just finish. And, finally, on a very specific issue, I would encourage the Court to go back and read paragraph four in Ambac's pleading in support of COFINA where it, with respect to specifically Section 314, focuses on a substantive difference, and notes -- between the Bankruptcy Code and PROMESA, and says, in putting that provision in, Congress recognized Puerto Rico's mixed sovereign status, and squarely put in this Court's

jurisdiction the ability to review and confirm the validity of Commonwealth law. And notes that the entirety of PROMESA has passed in connection and in conjunction with the Territories Clause. And I think that completely undermines the idea that there's nothing inconsistent about the position they're taking now and the position they took then.

Thank you, Your Honor.

THE COURT: Thank you, Mr. Friedman.

And, Mr. Bienenstock, we have you allocated for 11 minutes.

MR. BIENENSTOCK: Thank you, Your Honor.

I was heartened by the number of things Ambac is not contesting. We explained that whether a law is a local law depends on whose debt is being dealt with. It's Puerto Rico's debt and its instrumentalities. Whose property? It's their property. Not what creditors -- where creditors are on any night all around the world, because it makes no sense that you can go from a local to a national to an international statute based on where the creditors holding debt happened to be.

And there was no answer to the fact that in *Binns*, the tax was imposed on anyone all around the world who owned a business needing a license in the territory of Alaska at that time.

THE COURT: I recognize -- but I heard her argue quite forcefully about national economic effects and effects

on markets in arguing for uniformity. So, you know, that may have been an indirect way of responding. I'll have to reflect on all of this more thoroughly of course.

MR. BIENENSTOCK: Right. And in response to that, Your Honor, there is -- every transaction in commerce is going to affect supply and demand, which ultimately affects everything else. We think that's a -- that argument has never been picked up by federal jurisprudence, as to what makes a statute local or national.

In terms of the argument that Chapter Nine is national, yes, because it applies across the United States to every municipality and governmental unit, other than the states themselves. Title III is just the opposite. It applies to only territories, and according to Ambac, only one territory, Puerto Rico.

Now, in terms of a key assertion that we explained in our briefs and in argument this morning, that Congress can pass local laws using what power the state would have, in this case, the Puerto Rico territorial government and Congress' general powers. And to support that, we took the language from the *American Insurance* case which said, in legislating for them, Congress exercises the combined powers of the general and of the state government. And that language was picked up and endorsed yet again in *Northern Pipeline*, as I explained earlier.

Ambac has no answer. They simply flip back to the party line: No, the state government can't do it; it can't be local. And that's just contrary to the law. Then what they say is they tie that to the Supreme Court's decision striking down or affirming the First Circuit, which struck down the Debt Enforcement Act in Puerto Rico.

That is not a viable argument for Ambac. And the reason is that Justice Thomas begins the Supreme Court's decision in that case with a paragraph that says, basically, the issue is whether the Federal Bankruptcy Code preempts state bankruptcy laws that enable insolvent municipalities to restructure their debts over the objections of creditors, and instead requires municipalities to restructure such debts under Chapter Nine of the Bankruptcy Code. And Justice Thomas cites 11 U.S.C. 903(1), which is the statute that the Supreme Court said prohibited Puerto Rico from passing its own statute.

Clearly, Ambac cannot have a meritorious argument in saying Congress can't use its own power, because it passed a statute that denied other states or territories of that power. If Congress -- Congress can enact that statute and can repeal that statute. So Ambac is basically arguing that Congress disqualified itself from being able to pass Title III by telling other jurisdictions they can't do it. Well, Congress doesn't have to disqualify itself, and clearly that was not

its intention. It's completely counter productive.

As far as the functional test, Your Honor, as Ambac admitted this morning, the functional test comes out of the *Boumediene* case that it cites, and the *Boumediene* case explicitly, explicitly relies on the Insular Cases, which are exactly the cases the Oversight Board and all of the other parties in support of the Motion to Dismiss disavowed relying on. And it's interesting, because Ambac accuses us in its brief of relying on the Insular Cases, which we expressly disclaimed, and then it relies on *Boumediene*.

But the second point on the functional test is, you know, Ambac said again this morning, so what's so bad about applying the Uniformity Clause, you know, great for commerce, great for this, great for that. And that's the problem with the functional test: Anything you like you say applies.

Well, different people will have different opinions as to whether it's actually beneficial to the United States of America and its territories to impose on territories the same laws you imposed on other municipalities. At the very minimum, that's debatable. And that's the problem with the functional test. It comes out whichever way you want it to come out, depending on your point of view. So there's no objectivity, no test, nothing that could lead nine courts out of ten, or even seven out of ten, to come out the same way, because it's all subject to whether -- what policies you

believe should be furthered and what policies are hindered.

In terms of Ambac's arguments that there was this growing recognition of the meaning of PROMESA, and the Oversight Board's increasing, I guess in their view, more extreme powers -- I mean, the uniformity question cannot be decided based on Ambac's private beliefs or its characterizations of what it thinks the Oversight Board was doing. There was no answer whatsoever to the fact that PROMESA doesn't have any priority provision that changes the priority of Ambac's claims from what they would be in Chapter 9 or Chapter 11. As I said earlier, Title III incorporates the exact same, identical, unfair discrimination statute as applies in Chapter 9 and Chapter 11.

Instead of answering on the merits, Ambac just lapses back to its overarching descriptions of its mindset, which is it thinks that we're going overboard or some such thing. But that's not law. That's just ranting against something they don't like.

And as far as feeling that their property interests are treated differently, and that's why we need a -- uniformity in position, let's look at the record. They asserted rights under Bankruptcy Code Section 928. This Court and the First Circuit rejected their contentions. They applied for cert to the Supreme Court, and it was denied. It wasn't a matter of Title III changing their property rights.

It was the fact that they didn't have the rights they thought they had.

(Sound played.)

MR. BIENENSTOCK: And they were governed by the same provisions as would be in the other chapters.

In the -- as far as their argument that the holistic approach is what's different in Title III, the First Circuit and this Court have said in the decisions on the 926 Trustee issues that they were taking from Chapter Nine cases the holistic approach. So Ambac has stepped into a trap it made by itself. It says the holistic approach makes it nonuniform. That was taken from the chapters that they say should apply here. And they're just a hundred percent wrong in their assertions.

As far as 106(e), the fact that fiscal plan certifications cannot be reviewed by the Court says nothing about confirmation of a Chapter 11 plan. And they had no answer to the fact that, as I explained at length earlier, in the *Blanchette* case, the Interstate Commerce Commission made major determinations about value, allocation, capitalization, public interest; and that, the Supreme Court said, did not make the Rail Act nonuniform with Section 77.

Ambac has no answer for that. They just repeat the argument they started with, that they don't like 106(e), and they don't like the fact that 314(b)(7) says the plan of

adjustment needs to be consistent with the fiscal plan. All the Board gets to do there is say how much debt it believes can be sustained by the reorganized debtor. And, frankly, if any debtor ever got up before Your Honor and said, Your Honor, I don't think I can carry more than X debt --

(Sound played.)

MR. BIENENSTOCK: -- I respectfully submit, Your Honor would not believe that plan is feasible if its proponent is saying, I can't afford it. And that's all 314(b)(7) does.

I guess my time has run out, so subject to any of the Court's questions, I'm concluded, Your Honor.

THE COURT: Thank you, Mr. Bienenstock. I don't have further questions for you. And so I thank you and all of the counsel who've presented excellent, clear arguments that give the Court much more food for thought, in addition to the extensive briefing that has been filed.

I take this motion under advisement, and this concludes today's hearing. I would like to note, for everyone's benefit, that there have been some inaccurate press reports that there is a hearing scheduled for February 10th. So please be aware, and I ask any press representatives who may be listening in to note that no hearing has been scheduled for February 10th. That is a submission deadline. That is not a hearing date.

The next scheduled hearing is the hearing concerning

Omnibus Claim Objections, which will be held on January 14th, this Thursday, beginning at 9:30 AM Atlantic Standard Time, which is 8:30 AM Eastern Standard Time, with the usual telephone observation units. There is a procedures order on file.

As always, I want to thank the marvelous court staff in Puerto Rico, Boston, and New York. They do constant, effective, efficient work in preparing for and in supporting the conduct of these hearings, and all of the administration of these cases. So thank you to the staff, as well as to counsel who argued today. That concludes my remarks.

I urge everyone to stay safe and keep well. And get a vaccine as soon as you're eligible. Take care, everyone. Thank you.

(Proceedings concluded.)

* * *

U.S. DISTRICT COURT)

DISTRICT OF PUERTO RICO)

I certify that this transcript consisting of 98 pages is a true and accurate transcription to the best of my ability of the proceedings in this case before the Honorable United States District Court Judge Laura Taylor Swain on January 12, 2021.

S/ Amy Walker

Amy Walker, CSR 3799

Official Court Reporter